

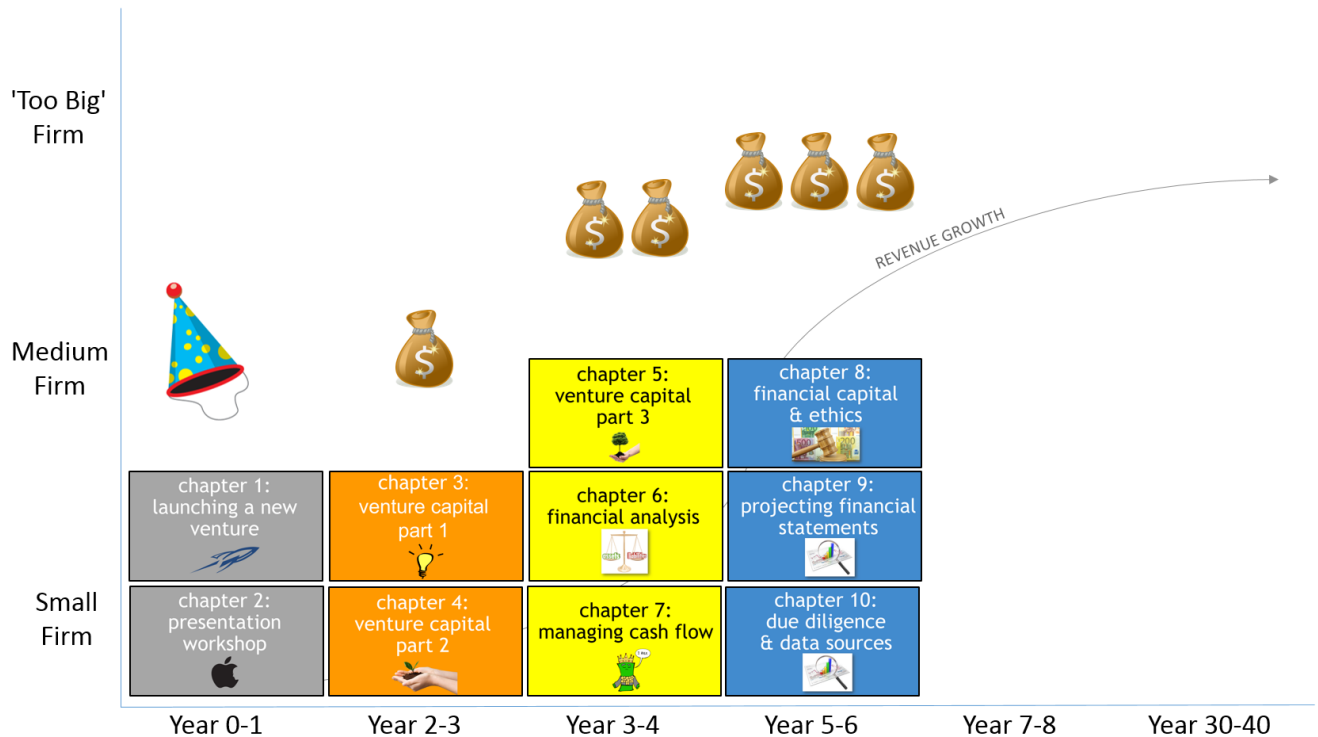
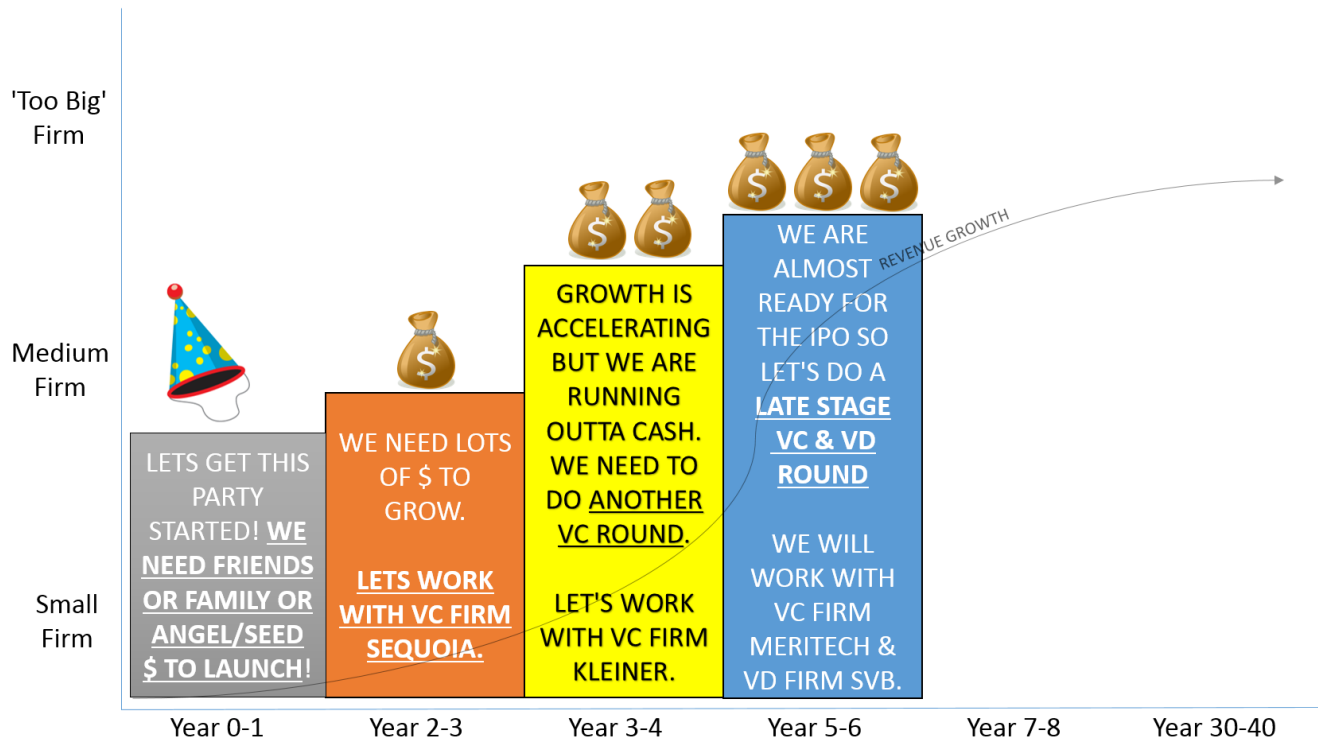
CHAPTER 10: DUE DILIGENCE AND DATA SOURCES

“What gets measured gets managed.”

- *Peter Drucker*

chapter 10:
due diligence
& data sources





Always do your own research. Always do your own due diligence. Everyone else has a bias and they want to influence your opinion. Please please please don't let anyone rent space in your head. Do your own work.

great financial analysts...

form their own opinions.

others have hidden agendas...

...but most are wrong.



great analysts don't let...

the following influence them

media.

other financial analysts.

folks that sound confident.

or...

politicians.



:)

in finance, please remember

confidence does not =

competence.

don't let others influence...

your opinion in finance.

be careful as...

CFOs are great salespeople.

how to tell if a CFO is lying?

when he moves his lips!

:)

be able to filter news from noise.

www.tiny.cc/chris78 :)

question the financial data
and
form your own opinion

foundations toolbox

qualitative.

quantitative.



every chart tells a story.

ORACLE®

oracle income statement.





oracle p/e chart.



10 year p/e multiple contraction!

negative organic growth!

ORACLE

~\$50bn in acquisitions since 2004



You need to understand why companies do what they do ('market signals'). Why is Oracle buying a massive tech company every year? Because the company is so big that organic revenue (its core competency) is actually contracting! Others will tell you otherwise. Just do your own research.

Don't rely on people that seem to speak gooder than you do :)

Every financial model that you create when analyzing a company is different as different companies have different revenue drivers for your model.

tech model i.s. drivers.

- ✓ subscribers or license revenues
- ✓ bookings
- ✓ operating and gross margin trends



tech model b.s.

- ✓ usually low debt if any
- ✓ cash rich
- ✓ analyze deferred revenue

In technology investing, balance sheets aren't usually too relevant as most technology companies don't have massive debt positions (you don't need factories to sell software on the Internet). We tend to analyze deferred revenue a lot with tech companies. What is deferred revenue? It is revenue that you can't recognize today. Huh? Well you can

only account or record revenue on your income statement when you get the benefit of selling the product in this financial period. Huh huh? Well if you sell 1 years worth of software today and your customer will pick up only 1 box of software this quarter and will come back to pick up the other box next quarter, then the box not picked up becomes deferred revenue so that you can only account for it in next quarter's financial statements (and not in this quarter's financial statements). Until then it is a liability on your balance sheet. Once you recognize it in your income statement then it is no longer a liability.

tech model c.f.

- ✓ usually tracks net income
- ✓ important for subscription companies
- ✓ some companies are seasonal.

Since tech companies don't usually have much debt, then cash flow is usually very close to net income.....so we don't have to bother creating a cash flow statement! Yep that's right.

You always want to model at least 5 years into the future. Ask yourself this basic question before doing any due diligence: "In 5 years is this company going to be more relevant or less relevant than it is today?" If you do this then you will make a killing owning companies like Amazon or LinkedIn and not lose your shirt shorting these companies in a bull market! Huh? Well in my LinkedIn financial model, I can get to \$50 in earnings in 5 years so LinkedIn's stock is only trading at 5x my 5 years earnings per share (EPS) estimate and is a bargain! Well if I looked at LinkedIn and Amazon on this year's earnings (bad idea) then I would think that both companies are ridiculously expensive.

what about valuation?

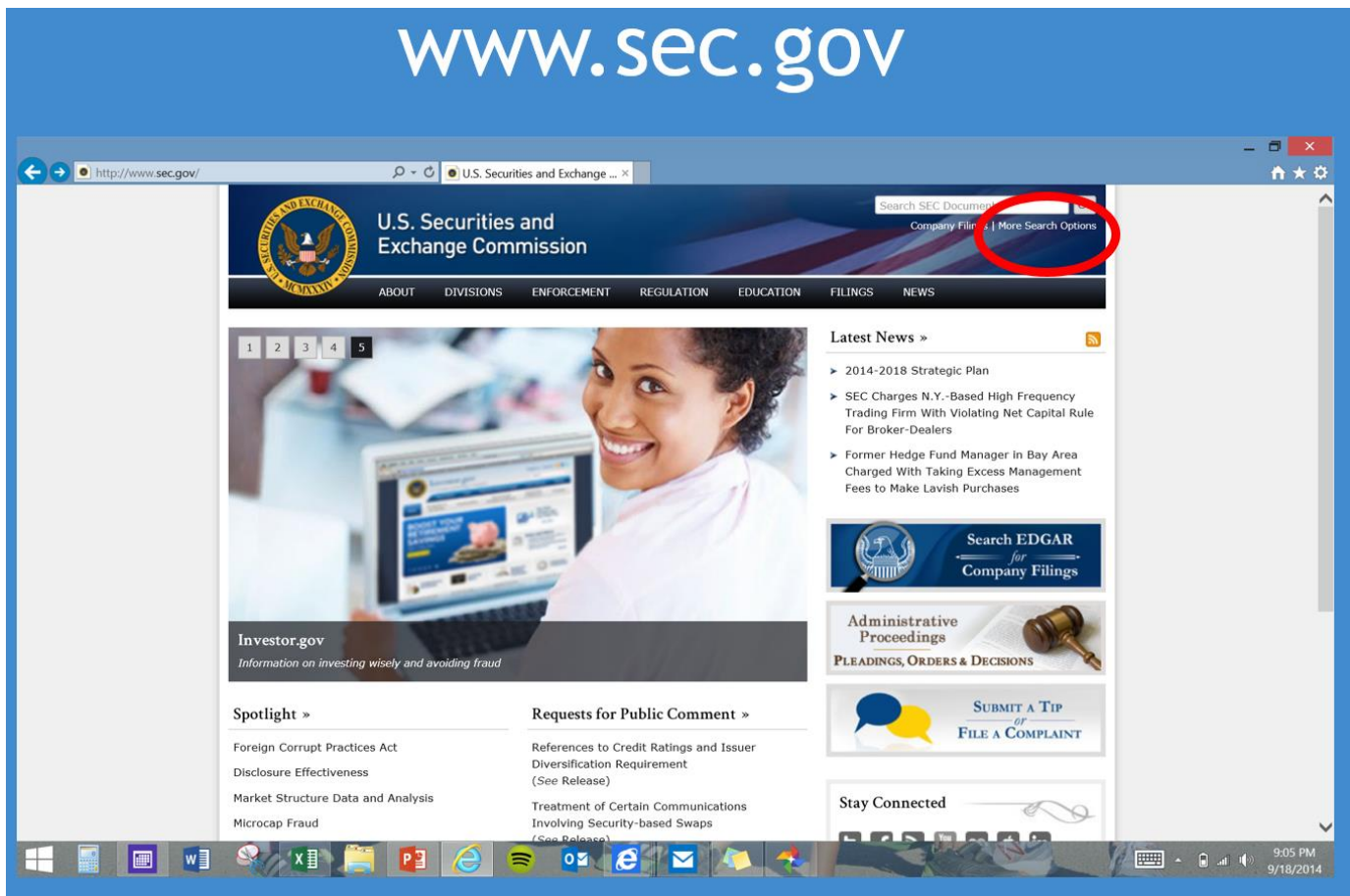
- ✓ value investors suck at tech.
- ✓ smart money models 5+ years out.
- ✓ use revenue, eps and cf multiples.

If you are valuing non tech companies, you still want to look 5 years out but you might be more inclined to make a discounted cash flow analysis instead of a p/e or p/sales based target price.

We already know that the best accounting resource on the web is www.sec.gov. Use this resource a lot to get detailed financial information on every publically traded company. We will do this in great detail next chapter.

what about non tech valuation?

- ✓ dcf
- ✓ smart money models 5+ years out.
- ✓ use revenue, eps and cf multiples.



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10-Q	Documents Interactive Data	Quarterly report (Sections 13 or 15(d)) Acc-no: 0000051143-14-000007 (34 Act) Size: 25 MB	2014-07-29	001-02360 14999420
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S-8	Documents	Securities to be offered to employees in employee benefit plans Acc-no: 0001104659-14-045837 (33 Act) Size: 156 KB	2014-06-13	333-106722 14909067
8-K	Documents	Current report, item 8.01 Acc-no: 0001104659-14-043338 (34 Act) Size: 21 KB	2014-06-02	001-02360 14884413
SD	Documents	Acc-no: 0001104659-14-043107 (34 Act) Size: 469 KB	2014-06-02	001-02360 14882340

This is a wealth of resources for all relevant quantitative and qualitative stuff. We will talk much more about this next chapter.

Questions Based on Chapter 10:

1: When doing due diligence on a company, it's important to:

- a) Do your own research and form your own opinion.
- b) Listen to the experts because their opinion becomes your opinion.

2: Value investors only buy expensive stocks.

True or False

3: The best investors value companies based on estimates in 5+ years.

True or False

CHAPTER SUMMARY



Chris Haroun @chris_haroun

quantitative tools = target price based on estimates in 5 years. look for trends. form your own opinion on all investments. DON'T LISTEN TO OTHERS! Sec.gov = great resource



this topic is worth repeating...

are you looking for a job?

Don't send in your resume anymore. Huh? It's too competitive and you have similar chances of winning the lottery. You need to set up many informational meetings using LinkedIn.

Every year I tell my students during the first day of class that I could guarantee them a job if they do 20 informational meetings with strangers at firms that they want to work for during the school semester. I ask them all who would do this if I would guarantee that you got the job of your dreams? Of course every single hand goes up! Then during the last class, I ask how many students actually did this? Usually only 1 or 2 hands go up and these students always get a great job! They are never the top students in the class either. Remember the Steve Jobs video. If you want something in life you need to ask for it! Ask and you shall receive.

be persistent on  and ask to please meet for a coffee. say you are a student.

to do: set up informationals.

how?

find something in common.

just ask.

people love helping students.

The screenshot shows the LinkedIn search interface. The search bar at the top contains the text "Moscow". On the left sidebar, under the "SEARCH" section, the "Keywords" filter is set to "Moscow", the "Company" filter is set to "Apple", and the "Within" distance filter is set to "100 mi (160 km)". The main content area displays "20 results for Moscow" with filters for "1st Connections", "2nd Connections", "Group Members", and "3rd + Everyone Else". The results list includes profiles for John Turnberg, Nate Johanningsmeier, Vyacheslav Malyugin, Anton D., Masha Markgraf, and Thom Franklin. Each profile shows their current position, past roles, education, and a "Connect" or "Send InMail" button.

SEARCH

Advanced >

All
People
More...

Keywords
Moscow

First Name
Last Name
Title

Company
Apple
Current
School
Location
Located in or near:
Country
United States
Postal Code
94010 Lookup

Within
100 mi (160 km)

Search Reset

20 results for **Moscow**

1st Connections x 2nd Connections x Group Members x
3rd + Everyone Else x Reset

John Turnberg 2nd
Searching for great Mechanical Engineers
San Francisco Bay Area • Internet
6 shared connections • Similar
Past: Technical Sourcer for Engineering at Google
Contractor working on the Diversity Sourcing team... the globe (Sydney, Moscow, Tel Aviv, Zurich, London...)
Current: Senior Technical Recruiter at Apple
Education: East longmeadow High School
University of Massachusetts, Amherst

Nate Johanningsmeier 2nd
Audio Hardware EE Manager at Apple Inc.
San Francisco Bay Area • Semiconductors
1 shared connection • Similar
Education: Московский Государственный Университет им. М.В. Ломоносо...

Vyacheslav Malyugin 2nd
Software Engineer at Apple, Inc
San Francisco Bay Area • Computer Software
2 shared connections • Similar
Education: Moscow State University

Anton D. 3rd
Software Engineer at Apple
San Francisco Bay Area • Computer Software
Similar
Past: Reporter Intern at The New York Times Moscow Bureau

Masha Markgraf 3rd
Linguistic Tester at Welocalize
San Francisco Bay Area • Entertainment
Similar
Current: Linguistic Tester at Apple/WeLocalize
Past: Picture Editor/Producer at Time Out Moscow
Education: Lomonosov Moscow State University

Thom Franklin 3rd
Program Manager at Apple
San Francisco Bay Area • Computer Software
Similar

www.tiny.cc/chris79



these people are no smarter
than you. they are successful
because they networked.



Confidence is not an American thing....but it is fascinating how American students (whether or not they were born in the US) are the most confident and with confidence comes the ability to sell yourself, raise money, reinvent an industry....etc. Please read the section on confidence in the last chapter of this book for more details on this crucial concept.

no smarter than you.